

Message Text

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FM AMEMBASSY KUALA LUMPUR

TO SECSTATE WASHDC 1676

INFO AMCONSUL HONG KONG

AMEMBASSY BANGKOK

AMEMBASSY JAKARTA

AMEMBASSY MANILA

AMEMBASSY SINGAPORE

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E.O. 11652: N/A

TAGS: EFIN MY

SUBJ: MALAYSIA: STATE OF THE ECONOMY AND 1976 BUDGET

MESSAGE TO PARLIAMENT

1. SUMMARY. DEPUTY PRIME MINISTER AND MINISTER OF FINANCE
HUSSEIN ONN PRESENTED GOM STATE OF THE ECONOMY AND 1976
BUDGET MESSAGE TO PARLIAMENT ON NOVEMBER 6. GNP IN 1975
GREW ONLY ONE TO TWO PERCENT IN REAL TERMS, AS EXPORT VALUES
DECLINED 11 PERCENT AND IMPORT VALUES 6.5 PERCENT IN CURRENT
PRICES. INFLATION REDUCED TO 7 PERCENT.

1975 CURRENT BUDGET EXPENDITURES EXCEEDED
ESTIMATES BY ABOUT M\$405 MILLION (US\$1.00 EQUALS
M\$2.50) DUE TO ADDITIONAL EXPENDITURES ON SECURITY AND
DEFENSE, RUBBER STABILIZATION SCHEME, SUBSIDIES FOR TEXT
BOOKS, AND GOVT. SALARIES INCREASES AND BONUSES. FOR 1976
GNP EXPECTED GROW 6 PERCENT IN REAL TERMS AND PRIVATE SECTOR
ENCOURAGED PLAY MORE EXPANSIONARY ROLE (PRIVATE SECTOR WAS
DISAPPOINTMENT IN 1975). HUSSEIN ONN DWELT AT LENGTH ON GOM
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POLICY OF ENCOURAGING PRIVATE INVESTMENT, DOMESTIC AND FOREIGN.

(THIS ASPECT BEING REPORTED SEPTEL.) FOR FIRST TIME, GOM PROJECTING SMALL DEFICIT IN CURRENT ACCOUNT IN 1976 BUDGET WHICH DOES NOT INCLUDE PROVISIONS FOR ADDITIONAL EXPENDITURES FOR SECURITY AND DEFENSE, SUBSIDIES, GOM SALARY INCREASES AND BONUSES, OR RUBBER PRICE STABILIZATION SCHEME. DEVELOPMENT ACCOUNT EXPENDITURES (PROJECTED M\$1,983 MILLION) DO NOT INCLUDE NEW PROJECTS OR PROGRAMS UNDER THIRD MALAYSIA PLAN, WHICH IS SCHEDULED TO BE PRESENTED TO PARLIAMENT IN MARCH 1976. 1976 BUDGET IS, IN EFFECT, A PARTIAL BUDGET WHICH GIVES GOM MUCH LATITUDE FOR REVISIONS DURING 1976. GOM CAN BE EXPECTED CONTINUE TO USE ITS LARGE FOREIGN EXCHANGE RESERVES AND FAVORABLE LONG-TERM OUTLOOK AS LEVERAGE FOR ADDITIONAL BORROWING FROM DOMESTIC AND FOREIGN MONEY MARKETS IN 1976 TO FINANCE EXPECTED DEFICITS. END SUMMARY.

2. DEPUTY PRIME MINISTER AND MINISTER OF FINANCE HUSSEIN ONN PRESENTED THE GOVERNMENT'S STATE OF THE ECONOMY AND 1976 BUDGET MESSAGE TO PARLIAMENT ON NOVEMBER 6. SPEECH REVIEWED THE ECONOMY AND FEDERAL BUDGET IN 1975; MADE PROJECTIONS ON ECONOMY IN 1976; AND OUTLINED 1976 BUDGET. PRINCIPAL POINTS OF MESSAGE ARE:

A. REVIEW OF 1975 ECONOMY. GNP GREW BY ABOUT ONLY ONE TO TWO PERCENT IN REAL TERMS AND GDP INCREASED ABOUT TWO AND ONE-HALF PERCENT. (PREDICTIONS AT END OF 1974 WERE FOR GNP GROWTH OF FIVE TO SIX PERCENT REVISED DOWNWARD AT MID-YEAR TO THREE TO FOUR PERCENT.) THIS IS ABOUT LOWEST GROWTH RATE MALAYSIA HAS HAD AND REFLECTS WORLD RECESSION. INFLATION ESTIMATED INCREASE SEVEN PERCENT COMPARED TO 17.4 PERCENT IN 1974. EXPORT VALUES DECLINED ELEVEN PERCENT IN CURRENT PRICES AND IMPORT VALUES DECLINED ABOUT 6.5 PERCENT IN CURRENT PRICES. BALANCE OF PAYMENTS MERCHANDISE ACCOUNT REGISTERED A DEFICIT FOR FIRST TIME IN RECENT YEARS. CURRENT ACCOUNT DETERIORATED BY ABOUT M\$1,285 MILLION WITH SERVICE ACCOUNT REGISTERING DEFICIT OF ABOUT M\$1,060 MILLION. BASIC BALANCE OF PAYMENTS NOW ESTIMATED BE ABOUT IN EQUILIBRIUM WITH OVERALL BALANCE OF PAYMENTS SHOWING DEFICIT OF ABOUT M\$100 MILLION. (COMMENT: INCREASED GOVT. MARKET BORROWINGS NARROWED DEFICIT.)

B. 1975 BUDGET. DESIGNED TO BE COUNTER-CYCLICAL WITH PUBLIC SECTOR EXPENDITURES ESTIMATED INCREASE ABOUT SEVEN PERCENT

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IN REAL TERMS AND PRIVATE SECTOR ABOUT FOUR PERCENT IN REAL TERMS. GOVT. SECTOR SPENDING IN FACT INCREASED BY ABOUT NINE PERCENT WHILE PRIVATE SECTOR SPENDING DECLINED BY ABOUT FIVE PERCENT.

C. 1975 BUDGET EXPENDITURES AND REVENUES. ACTUAL AMOUNT EXPENDITURES EXCEEDED ESTIMATED EXPENDITURES BY ABOUT M\$405 MILLION DUE TO FOLLOWING EXPENDITURES WHICH WERE NOT ANTICIPATED: (1) M\$127 MILLION FOR SECURITY AND DEFENSE, (2) M\$40 MILLION FOR

RUBBER STABILIZATION SCHEME, (3) M\$26 MILLION FOR TEXT BOOKS
SUBSIDY, (4) M\$250 MILLION FOR GOVT. SALARY INCREASES AND BONUSES.
WITH LOWER REVENUES 1975 CURRENT ACCOUNT EXPECTED RECORD DEFICIT
OF M\$135 MILLION. DEVELOPMENT EXPENDITURES EXCEEDED 1975 BUDGET
ESTIMATES BY ABOUT M\$235 MILLION RESULTING IN OVERALL BUDGET
DEFICIT OF M\$2,035, HIGHEST EVER RECORDED IN SMP PERIOD.

D. ECONOMIC OUTLOOK FOR 1976. EXPECT FAVORABLE FIRST HALF
WITH FURTHER IMPROVEMENT IN SECOND HALF FOR 1976 REAL INCREASE
IN MALAYSIAN GNP OF 6 PERCENT. EXPORTS ESTIMATED GROW BY ABOUT
NINE PERCENT AND IMPORTS BY ABOUT FIVE PERCENT IN REAL TERMS.
RUBBER ACCOUNTS FOR ABOUT 16 PERCENT GDP AND HAS SUBSTANTIAL
IMPACT ON ECONOMIC GROWTH AND SOCIO-ECONOMIC WELL BEING OF NEARLY
THREE MILLION MALAYSIANS. REASONABLE TO ASSUME AVERAGE PRICE OF
ABOUT 140 MALAYSIAN CENTS PER KILO FOR RSSI RUBBER IN 1976.
PRIVATE SECTOR SHOULD PLAY MORE POSITIVE AND EXPANSIONARY ROLE.
GOM UNDERSTANDS THERE IS SOME UNCERTAINTY REGARDING GOVT.'S
POLICIES TOWARDS PRIVATE INVESTMENT; GOM WISHES TO STATE CATEGOR-
ICALLY THAT IT WELCOMES AND INDEED ENCOURAGES PRIVATE INVESTMENT.
(SEE SEPTTEL ON PRIVATE INVESTMENT ASPECTS OF SPEECH.)
GOVT. WILL HAVE TO CONTINUE PLAY LEADING AND COUNTER-CYCLICAL
ROLE WHILE BEARING IN MIND NEED TO MAINTAIN FINANCIAL STABILITY.

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ACTION EA-09

INFO OCT-01 ISO-00 STR-04 AID-05 CIAE-00 COME-00 EB-07

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E. 1976 BUDGET. DIVIDED INTO CURRENT ACCOUNT AND DEVELOPMENT ACCOUNT. CURRENT ACCOUNT IS ESTIMATED TO HAVE DEFICIT OF M\$82 MILLION WITH REVENUES PROJECTED AT M\$5,258 MILLION (ABOUT SIX PERCENT OVER 1975) AND ORDINARY EXPENDITURES AT M\$5,340 (INCREASE OF SEVEN PERCENT COMPARED 1975) AND ADJUSTMENT OF M\$50 MILLION TO SINKING FUND. ESTIMATED DEFICIT IN CURRENT ACCOUNT DOES NOT INCLUDE PROVISIONS FOR ADDITIONAL EXPENDITURES FOR SECURITY AND DEFENSE (M\$127 MILLION IN 1975); SUBSIDIES, WHICH IN 1975 AMOUNTED TO M\$183 MILLION (M\$88 MILLION FOR RICE AND M\$50 MILLION FOR UREA); GOVT. SALARY INCREASES AND BONUS PAYMENTS (M\$250 MILLION IN 1975); NEW POSITIONS, OR ANY OTHER POLICY DECISIONS WHICH HAVE FINANCIAL COMMITMENTS (E.G., RUBBER PRICE STABILIZATION SCHEME). DEVELOPMENT EXPENDITURE (M\$1,983 MILLION) IS TENTATIVE PENDING FINALIZATION OF THIRD MALAYSIA PLAN (TMP) AND DOES NOT INCLUDE ANY NEW PROGRAMS OR PROJECTS UNDER TMP. TENTATIVE OVERALL BUDGET DEFICIT PROJECTED AT ABOUT M\$2,065 MILLION TO BE FINANCED BY DOMESTIC BORROWING ESTIMATED AT M\$1,300 MILLION AND FOREIGN PROJECT AND MARKET BORROWING ESTIMATED AT ABOUT M\$725 MILLION, PLUS SPECIAL RECEIPTS OF M\$40 MILLION.
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F. TAX PROPOSALS FOR 1976. INCREASES IN TAXES AND DUTIES EXPECTED PRODUCE ADDITIONAL REVENUES OF M\$108 MILLION. RATES OF DIRECT TAXES OF INDIVIDUAL INCOME TAX, REAL PROPERTY GAINS TAX, AND ESTATE DUTY HAVE BEEN REVISED UPWARD. INDIRECT TAXES OF IMPORT DUTIES ON LUXURY ITEMS INCLUDING FRESH, DRIED, AND PRESERVED FRUITS; CARS AND MOTORCYCLES; MUSICAL INSTRUMENTS AND HI-FI EQUIPMENT; AND PERFUMES, COSMETICS, AND TOILETRIES ARE INCREASED. PENANG ISLAND LOSES RESIDUAL OF FREE-PORT STATUS. SURTAX OF FOUR PERCENT ON ALL IMPORTS EXCEPT CERTAIN ESSENTIAL GOODS INCREASED TO FIVE PERCENT WITH PARTIAL EXEMPTION FOR RAW MATERIALS NEEDED BY MANUFACTURERS. EXCISE DUTY ON LOCALLY ASSEMBLED AUTOMOBILES ALSO RESTRUCTURED UPWARD.

3. COMMENT. 1976 BUDGET, IS IN FACT, A PARTIAL BUDGET AS IT DOES NOT INCLUDE PROVISIONS FOR ADDITIONAL EXPENDITURES FOR SECURITY AND DEFENSE, WHICH PROBABLY WILL BE SIGNIFICANT; SUBSIDIES, WHICH AMOUNTED TO M\$183 MILLION IN 1975 BUT COULD DECLINE; RUBBER PRICE STABILIZATION SCHEME (M\$40 MILLION IN 1975), WHICH COULD EXCEED 1975 FIGURES WHICH AGREEMENT EFFECTED BY ASSOCIATION OF NATURAL RUBBER PRODUCERS; AND NEW PROJECTS AND PROGRAMS UNDER THIRD MALAYSIA PLAN, WHICH SCHEDULED FOR PRESENTATION TO PARLIAMENT IN MARCH 1976. EVEN WITHOUT INCLUSION THESE ITEMS, GOM PROJECTS A CURRENT ACCOUNT DEFICIT FOR FIRST TIME IN MALAYSIA'S HISTORY. GOVT. HAS GIVEN ITSELF WIDE LATITUDE IN PROPOSED BUDGET AND REVISIONS CAN BE EXPECTED THROUGHOUT 1976, ESPECIALLY

DURING FIRST HALF OF YEAR, DEPENDING LARGELY ON ECONOMIC RECOVERY OF DEVELOPED COUNTRIES. WE ALSO EXPECT GOVT. TO CONTINUE PRACTICE OF BORROWING IN FOREIGN MONEY MARKETS, AS IT HAS DONE IN 1975 TO TUNE OF ABOUT US\$425 MILLION, AND TO USE ITS FOREIGN EXCHANGE RESERVES OF ABOUT M\$3,790 MILLION AND LONGER-TERM FAVORABLE OUT-LOOK AS LEVERAGE FOR THESE BORROWINGS. AS PRESENTED, 1976 BUDGET IS CONSERVATIVE AND WILL NOT PROVIDE MUCH EXPANSIONARY THRUST BUT, AS NOTED ABOVE, ALL PROJECTED EXPENDITURES ARE NOT INCLUDED. NEW DEVELOPMENT EXPENDITURES IN TMP COULD PROVIDE MAJOR EXPANSIONARY BOOST TO ECONOMY. END COMMENT.
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